



1 July 12, 2007

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3 Memorandum

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5 To: Members of the Board

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7 From: Richard Fontenrose, Assistant Director

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9 Through: Wendy M. Comes, Executive Director

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11 Subject: Social Insurance,<sup>1</sup> Tab A

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14 This memorandum provides an overview of comments received on the *Preliminary Views*  
15 document, discusses areas where there appears to be consensus among members as well as  
16 areas where the members may differ, and explores alternatives for moving forward. The  
17 objective of this session is twofold: first, to present a plan for addressing social insurance; and,  
18 second, afford members an opportunity to provide tentative feedback regarding comments  
19 received and the work to date.

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22 I. Discussion of Respondents' Comments

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24 ***Preliminary Views Document***

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26 Sixty-seven respondents submitted comments to the *Preliminary Views* as follows:

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28 1. 18 federal government representatives:

- 29  
30 A. 5 users, academics, other  
31 B. 6 auditors  
32 C. 7 preparers and managers

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34 2. 49 non-federal representatives:

- 35  
36 D. 47 "users, academics, other"  
37 E. 2 "auditors"

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<sup>1</sup> The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

1 Attachment 1 provides a record of the responses received to the *Preliminary Views*  
2 document. Attachment 1, Table 1 (pages 10-11) summarizes the responses on each  
3 question. (Also, see Attachment 5 for the detailed worksheet used for Table 1.)  
4

5 The following is an overview of the comments received on each of the six questions  
6 asked in the *Preliminary Views* document. (See Box 1 below for a quick reference  
7 regarding the questions).  
8

9 1. Question 1 asked respondents which obligating event they favored. **A slight**

10 **majority of respondents** who commented  
11 on this question **favored either the**  
12 **Primary View (22) or “work in covered**  
13 **employment” (11). The Alternative View**  
14 **received the single most favorable**  
15 **responses among the four obligating**  
16 **event options (30). No respondents**  
17 commented on “threshold” eligibility.<sup>2</sup>

18 Attachment 1 (pages 3-6) lists examples of  
19 the reasons given by respondents for their  
20 decision regarding Question 1; also, an  
21 abstract of comments by question number  
22 is provided in Attachment 1, Table 2  
23 (pages 12-36). Generally, respondents  
24 supporting either the Primary or Alternative  
25 Views cite the rationale for each position in  
26 the *Preliminary Views* basis for  
27 conclusions. Those favoring the work-in-  
28 covered-employment obligating event often  
29 saw an exchange transaction occurring  
30 (payroll tax payments “in exchange” for  
31 future benefits), or saw no difference  
32 between SI and pensions. Some of those  
33 favoring work-in-covered-employment  
34 event stated that the government had  
35 created an expectation and reliance.

36 2. Question 2 asked if Social Security and Medicare obligations were measurable for  
37 the purpose of liability reporting at 40 quarters of work in covered employment as  
38 proposed in the Primary View. **A majority of respondents** who commented on this  
39 question **agreed with the Primary View (21 of 38)**. Examples of the reasons given  
40 by respondents for their decision regarding Question 2 are listed in Attachment 1,

Box 1 – PV Questions

1. Which obligating event creates a liability and expense for social insurance programs?
  - A. All work in covered employment regardless of “vesting”
  - B. “Substantially meeting eligibility requires,” which for Social Security and Medicare occurs when workers become “fully insured” at 40 quarters of or equivalent work in covered employment and subsequently as workers become eligible for additional benefits due to work in covered employment
  - C. “Threshold eligibility,” which for Social Security and Medicare occurs at 62 or 65 years of age when workers become permanently fully insured
  - D. “Due and payable”
2. Are Social Security and Medicare obligations measurable for the purposes of recording a liability after 40 quarters or equivalent work in covered employment?
3. Statement of Social Insurance (SOSI): Should line items be added to SOSI that tie to expense and liability amounts reported in the SNC and balance sheet per primary view (PV)? Should the reasons for changes in SOSI amounts be reported? If so, which approach is favored: PV? Alternative view (AV)?
4. Should a “statement of fiscal sustainability” be adopted?
5. Should “deferred revenue” be considered?
6. Other comments?

<sup>2</sup> Staff notes that its count of respondents’ opinions is approximate and subject to interpretation. Some respondents were difficult to classify. For example, Dr. Prince (letter 51) stated that he concurred with the Primary View but would not report the 40-QC liability on the balance sheet; he suggests limited disclosure instead. Staff counted Dr. Prince as favoring the Primary View regarding Question 1 but not regarding Question 2. Thus, the tally is a starting point for discussion rather than conclusive evidence.

- 1 page 6; and an abstract of comments is provided in Attachment 1, Table 2 (pages  
2 12-36).
- 3 3. Question 3 involved several components. Examples of the reasons given by  
4 respondents for their decision regarding Question 3 are listed in Attachment 1, page  
5 7; and an abstract of comments is provided in Attachment 1, Table 2 (pages 12-36).
- 6 3.1 Question 3.1 asked the respondents whether the Board should adopt the  
7 Primary View proposal to add line items to the Statement of Social Insurance (SOSI)  
8 that tie to revised liability and expense amounts in the primary statements. About  
9 **two-thirds** of the respondents who commented on this question (23 of 36) **did not**  
10 **agree with the Primary View**.
- 11 3.2 With respect to the question of reporting on SOSI changes (Question 3.2),  
12 almost everyone who commented **avored reporting on changes** (31 of 34).
- 13 3.3 A subcomponent of Question 3.2 asked those who favored reporting changes  
14 whether they preferred the Primary or Alternative View approach, and a **majority** (22  
15 of 31) **preferred the Alternative View** approach.
- 16 4. Question 4 asked respondents whether the Alternative View proposal to present a  
17 statement of fiscal sustainability in the Financial Report of the United States  
18 Government (FR) as required supplementary information (RSI). **A majority of**  
19 **respondents** who commented on this question **avored the Alternative View**  
20 **proposal** (29 of 41). Examples of the reasons given by respondents for their  
21 decision regarding Question 4 are listed in Attachment 1, page 7-8; and an abstract  
22 of comments is provided in Attachment 1, Table 2 (pages 12-36).
- 23 5. Question 5 asked respondents whether the Board should consider the Alternative  
24 View proposal regarding deferred revenue for earmarked revenues in excess of  
25 related program costs. **A majority of respondents** who commented on this question  
26 **did not agree with the Alternative View proposal** (20 of 33). Examples of the  
27 reasons given by respondents for their decision regarding Question 5 are listed in  
28 Attachment 1, page 8; and an abstract of comments is provided in Attachment 1,  
29 Table 2 (pages 12-36).
- 30 6. Question 6 asked respondents for any other comments they might have on the  
31 guidance provided for measurement, display, disclosure, and RSI. The respondents  
32 had various comments as shown in the Table 2 below. An abstract of comments is  
33 provided in Attachment 1, Table 2 (pages 12-36).

34 **May 23 Hearing**

35 Sixteen people testified on May 23 as follows (the minutes are present at Attachment 2):  
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- 37 1. 5 from federal government:  
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39 ○ Steven Schaeffer, SSA IG office  
40 ○ CG Walker  
41 ○ Steve Robinson from Senator Grassley's office  
42 ○ Stephan Goss, SSA chief actuary

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- Representative James Cooper
- 2. 11 from private sector:
  - Institutes/organizations:
    - Bob Bixby, Concord Coalition
    - Sheila Weinberg, Institute for Truth in Accounting
    - John Rother, AARP
    - Jagadeesh Gokhale, Cato Institute
    - Bob Childree, AGA FMSB
    - Alison Fraser, Heritage Foundation
  - Other:
    - Thomas Prince, NW University
    - Martha Zeilger, municipal government financial director, NC
    - Howell Jackson, Harvard Law School
    - Mike Shannon
    - Terry Menzel, KPMG
- 3. The following are staff notes regarding comments made at the hearing, organized by topic:
  - A. Obligating events:
    - 1. Work in covered employment (WICE):
      - Recognize a commitment to provide benefits for all beneficiaries, not just the very young, but he is indifferent as to what you call the commitment. (Gokhale)
      - Supports PV but believes beginning WICE is the point at which measurement should commence. There is an implicit exchange transaction when payroll taxes are paid. (Menzel)
    - 2. "Threshold" event:
      - Congress would be reluctant to change retiree benefits and, generally, retirees would need certainty. (Rother)
      - A reasonable period could be looked at. (Schaeffer)
    - 3. Due and payable:
      - Due and payable is appropriate and consistent with the liability definition in the *Elements* ED. The proposed Primary View (PV) cost would dwarf other costs. (Schaeffer)
      - The AV is more consistent with current law, Government SI communications, and international accounting. (Walker)
      - Current standard is consistent with current law.
  - B. Current law:

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- As long as the policy is in place, there is a liability. (Gokhale)
- The AV is consistent with current law. (Walker)

C. Congress' ability to change the law:

- Some commented that the key difference between the private sector and the government is Congress' ability to raise taxes and change benefits and the AV is a more accurate representation of this. (Rother, Walker)
- Current law expressly reserves the right to change or repeal SI programs, which is one of the two unique characteristics of Social Security and Medicare that make PV inappropriate. The other is the statutory limit on Trust Fund payments. (Robinson)
- Congress can change a great many things in addition to SI programs, including repudiating debt. Consideration of Congress' ability to change law is not very helpful in deciding whether something is recognized. (H. Jackson)
- Accounting measures liabilities based on the circumstances at the balance sheet date. The notion is embedded in the literature. (Menzel)

D. The meaning of "liability": Views differ regarding what constitutes "liability."

- "Liability" is equivalent to a "legal liability." (Bixby)
- Reporting a liability does not change legal status. (Zeigler)
- Liabilities are implicitly linked to funding and information in that context is not useful for evaluating SI, which is not (or cannot be) advance-funded. (Bixby, Robinson) This is appropriate for private companies that can go out of business but not for the Government, which is perpetual, nor for SI, for which the deficit is too large to pre-fund in any case. (Robinson)
- The Government's commitment to the Social Security Trust Fund (and other holders of US Treasury securities) is irrevocable and the Board should consider recognizing a deferred revenue liability. (Walker, Goss)
- A liability is something that must be paid yet we know Social Security benefits can be changed at any time and therefore classifying them as liabilities would be misleading. (Fraser)
- Language is important. The liability label makes benefits intractable. (Fraser)

E. The affect of reporting a long-term liability on efforts to reform Social Security and Medicare:

- Calling the SI commitment a "liability" may preclude reform due to the political perception of a repudiation of a debt. (Bixby)
- Reporting an accrued liability would make reform harder. (Weinberg)
- Reporting an accrued liability would be more likely to stimulate reform than impede it. (Zeilger, H. Jackson)

- 1                   ○ The outcome of the Board’s work is not expected to lead to the
- 2                   resolution of issues regarding the sustainability of programs.
- 3                   (Walker)
- 4                   ○ It are not just what you do but how you do it. It will be either a net
- 5                   plus or a net minus in improving public understanding, and the
- 6                   possible narrowing of options for reform. (Walker)
- 7                   ○ The acting of sending SSA individual statements has not “locked-in”
- 8                   benefits, and it is not plausible that reporting a gross number will
- 9                   accomplish that. (H.Jackson)
- 10                  ○ Citizens comprehend that a benefit is being accrued as they work.
- 11                  From a technical legal perspective, the PV would not “lock in”
- 12                  benefits. (Cooper)
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15                  F. The difference between SI and other federal programs:

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- 17                   ○ Prefers to start measuring fiscal condition from a governmentwide
- 18                   perspective and therefore Medicaid and other programs should be
- 19                   included. Start with a complete picture of the overall projection and
- 20                   then explain components of the continuum. (Gokhale)
- 21                   ○ SI programs are not different from other entitlement programs. SI
- 22                   commitments are similar to defense spending. How the government
- 23                   manages such spending to similar how individuals manage the
- 24                   family budget: child-rearing costs are not prefunded when the child
- 25                   is born. (Schaefer)
- 26                   ○ SI programs are more defined than other programs that might
- 27                   appear similar. (Walker)
- 28                   ○ There are many factors (trust funds, payroll tax, accumulation of
- 29                   benefits from being in the work force, open-ended appropriations)
- 30                   that distinguish SI programs from others. (H. Jackson)
- 31                   ○ Entitlement programs are the gray area on the “continuum.”
- 32                   Programs with mandatory spending fall on the liability side. It is
- 33                   easier to block changes than to put through changes. Permanent
- 34                   appropriations are hard to change and are somehow locked in.
- 35                   They are on “autopilot.” Yes, this makes funding key criteria but
- 36                   only in the sense that permanent appropriations are very hard to
- 37                   change. (H. Jackson)
- 38                   ○ SI is not welfare. SI gives the appearance that participants are
- 39                   paying for benefits. (Cooper)
- 40

41                  G. What a “liability” on the balance sheet would communicate:

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- 43                   ○ People may be confused if a liability amount differs from estimates,
- 44                   for example, the unfunded obligation, reported in the Trustees’
- 45                   Report. (Bixby)
- 46                   ○ A liability is a snapshot of where the program is. (Zeilger)
- 47                   ○ A liability is a different number than the “closed group” or “open
- 48                   group” number. These numbers measure different things. (Bixby)
- 49                   ○ A liability is only a part of the SI commitment and reporting it on the
- 50                   balance sheet could mislead users. (Gokhale)

- 1 ○ “Liability” and “balance sheet” may be accounting constraints that
- 2 work well in the private sector but not in the public sector; for
- 3 example, the use of shutdown measures when the program will not
- 4 be shut down. (Gokhale)
- 5 ○ The AV liability position is consistent with other Government
- 6 communications (benefit statements). (Walker)
- 7 ○ Some line must be drawn between what you call a liability and what
- 8 you do not. We should not represent SI – and perhaps not OPEB or
- 9 other uncertain future benefits either – as promises because of the
- 10 misunderstanding that it can create. (Goss)
- 11 ○ A liability should convey the magnitude of the commitment and the
- 12 change in fiscal burdens. (H. Jackson)
- 13 ○ It makes a difference whether you recognize an element on the
- 14 balance sheet or other statements or disclose it in notes. (Menzel)
- 15 ○ If you have a statement of financial position that does not include all
- 16 aspects of position then you are misleading people. (Menzel)
- 17 ○ The balance sheet is the only way to communicate with citizens on
- 18 this issue. Citizens consider the balance sheet a “real” financial
- 19 statement. For example, it would be meaningful to Rotarians.
- 20 Accounting must mesh with the people’s understanding. (Cooper)
- 21 ○ The financial statements should provide information for policy
- 22 decisions. With liability recognition, the immediate reaction is tax
- 23 increases. (Fraser)
- 24

25 H. The significance of payroll tax “contributions”:

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- 27 ○ Earmarked funds create a distinction among entitlement programs.
- 28 (Bixby, Weinberg)
- 29 ○ The public probably perceives payroll tax contributions as an
- 30 indication of an exchange transaction. (Bixby, Cooper)
- 31 ○ Payroll tax contributions are not directly tied to benefits. (Bixby)
- 32 ○ The payroll tax has little significance other than political. Parts of
- 33 Medicare are funded differently but have the same substance.
- 34 (Robinson)
- 35

36 I. Public perception of the commitment:

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- 38 ○ Look at the legality of the program not how the public perceives it.
- 39 (Bixby)
- 40 ○ What the public thinks based on what the politicians say is what
- 41 really matters. The public refers to SI as social contracts.
- 42 (Weinberg)
- 43

44 J. The statement of fiscal sustainability and/or non-traditional financial

45 statements:

- 46
- 47 ○ The Board may decide to call the balance sheet number something
- 48 other than “liability” but the number should be on the balance sheet,
- 49 and the change should be reported as a cost. The bottom line on
- 50 the SNC equates to the budget deficit and that is the number that
- 51 should be the focus. (Weinberg)

- 1                   ○ The key issue is to capture the full governmentwide and component
- 2                   effect of policy changes. (Gokhale)
- 3                   ○ The balance sheet is a snapshot in time and a statement of fiscal
- 4                   sustainability would help evaluate that point-in-time picture.
- 5                   (Zeilger)
- 6                   ○ Disclosure of the PV information is useful in the right context.
- 7                   (Schaeffer, Walker)
- 8                   ○ The fiscal sustainability report should be developed first to
- 9                   communicate the totality of the issue, followed by the liability
- 10                  standard. (Childree, Robinson) Something is needed that helps us
- 11                  understand what this really means in the grand scheme of things,
- 12                  and to decide whether a \$40-trillion number is appropriate. The
- 13                  standard needs to be generally accepted. (Childree)
- 14                  ○ A broad look at sustainability is needed, including all programs and
- 15                  sources of revenue. (Walker)
- 16                  ○ We need to think about whether a traditional balance sheet is
- 17                  meaningful for a national government. Important items are not on
- 18                  the balance sheet. The current deeply red condition of the federal
- 19                  balance sheet has not motivated anyone to do anything. Out-of-the-
- 20                  box thinking is needed. Perhaps combine traditional balance sheet
- 21                  with items from fiscal sustainability. (Walker)
- 22                  ○ FASAB should focus on improving SOSI and on sustainability
- 23                  reporting. (Robinson)
- 24                  ○ "Sustainability" is not well defined. Social Security is sustainable, for
- 25                  example, within the statutory limits. (Goss)
- 26                  ○ Integrating the amounts with current statements is very important.
- 27                  He referred to two models for linking amounts. Staying within the
- 28                  structure of traditional financial statements is helpful. Non-experts
- 29                  need a bottom line. There must be a single number to be
- 30                  understandable. He supports sustainability reporting but it
- 31                  addresses a different question. (H. Jackson)
- 32                  ○ Table 1 in the FR Executive Summary is excellent. (H. Jackson,
- 33                  Fraser)
- 34                  ○ The federal government is unique and it is worth considering
- 35                  whether the traditional balance sheet is helpful. (Menzel)
- 36

37                  K. The difference between the cost of federal employees and other

38                  administrative costs and SI costs:

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- 40                   ○ If the government enacted a policy that everyone gets \$50 then the
- 41                   cost of the policy is that amount. (Gokhale)
- 42                   ○ SI costs can be likened to insurance contracts where premiums are
- 43                   paid and policyholders expect a benefit there from; both should be
- 44                   recognized by the company. (Zeilger)
- 45

46                  L. Uncertainty:

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- 48                   ○ The amount of benefits is uncertain and estimates are unreliable.
- 49                   (Schaeffer)

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2 M. Measurement:

- 3  
4 ○ The amount should be net of future payroll taxes. (XXXX)  
5 ○ If the PV were adopted all flows should be considered. (Schaeffer)  
6 ○ Payroll taxes are used for other government expense they should  
7 not be subtracted. (Weinberg)  
8 ○ A comprehensive measure for all beneficiaries and for past and  
9 future events is preferable. (Gokhale)  
10 ○ The closed group obligation may be a useful compromise. It  
11 addresses the generation imbalance, increases over time due to  
12 implicit interest, and picks up statutory and demographic changes.  
13 Economists and actuaries are familiar with it. The closed group  
14 vested measure would be similar to how swaps are accounting for  
15 and could be useful. The fact that amounts are large should not be  
16 a deterrent. (H. Jackson)  
17 ○ There are no measurement issues with the PV proposal. (Menzel)  
18 ○ The PV would not offset future benefits with future payroll taxes,  
19 which would be misleading. (Fraser)  
20

21 Several respondents suggested alternative approaches. Mr. Jackson's proposal is at  
22 Attachment 3. Several people testified that Table 1 from the Financial Report of the  
23 United States' Executive Summary is good starting point for discussion of possible new  
24 reporting or new financial statements, and it is provided at Attachment 4.  
25

26 II. Majority of Respondents Favored Certain Positions  
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28 Although the respondents split on the obligating event and other issues, the tally of  
29 respondents' comment letters indicates that a majority of respondents may favor the  
30 following positions:  
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- 32 1. Social Security and Medicare obligations are measurable for the purposes of  
33 recording a liability after 40 quarters or equivalent work in covered employment.  
34 2. Line items should not be added to SOSI. The current format is preferred.  
35 3. The reasons for changes in SOSI amounts should be reported, and there should  
36 be a new basic statement for this purpose.  
37 4. A sustainability reporting should be developed either in the SI project or  
38 separately.  
39 5. Reporting "excess" payroll taxes as deferred revenue either is not favored or  
40 should not be a part of the SI project.  
41

42 III. FASAB Consensus  
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44 When the Board issued the *Preliminary Views* document there appeared to be a  
45 consensus among members regarding several points. The members agreed that the  
46 Statement of Social Insurance (SOSI) was a useful financial statement, and that changes  
47 in SOSI amounts should be reported. However, views appeared to differ regarding the  
48 display format of the SOSI and for changes in SOSI. In addition, the members agreed  
49 that sustainability reporting is necessary and a separate project commenced. Finally,  
50 they agreed that the supplementary information required in SFFAS 17 should be  
51 continued.

1  
2 On the other hand, views differed in other areas. The discussion of differing views may  
3 benefit from the following summary of the Primary View (PV) and Alternative View (AV)  
4 rationales from the bases for conclusions, focusing on the liability and associated issues.

5  
6 **Primary View**

7  
8 The PV is that the attainment of fully insured status (e.g., 40 QC) constitutes  
9 substantially meeting of eligibility requirements for Social Security and Medicare, and  
10 therefore is an obligating event and a present obligation. The PV basis for this  
11 conclusion notes that there is dissatisfaction with the SFFAS 17, “due and payable”  
12 liability and cites AICPA letters to this effect (PV par. A2). It also refers to economists  
13 and others expressing concern regarding the completeness of information. It cites Alan  
14 Greenspan on the benefits of accrual accounting (PV par. A4), and there are references  
15 to Fisher, Diamond, Orszag (PV par. A5) and Howell Jackson (PV par. A6).

16  
17 The PV is that decision-makers will benefit from PV information. The balance sheet  
18 would be closer to presenting total liabilities and the SNC much closer to presenting the  
19 cost of transactions and events occurring during the period. Citizens and intermediaries  
20 would gain access to information used by experts (PV par. A7).

21  
22 Pursuant to the liability definition in the *Elements* ED, a liability of the Government has  
23 two essential characteristics: (1) it constitutes a present obligation and (2) the  
24 Government and the other entity have an agreement or understanding as to when  
25 settlement is to occur. Present obligations require past obligating transactions or events;  
26 such events are critical for liability determination (PV pars. A12-A13). The existence of  
27 an obligation is determined with reference to current law (PV par. A14).

28  
29 Expenses include increases in liabilities (PV pars. A9-A11). The expense to be  
30 recognized is consistent with the SI benefit formula. (PV par. 55).

31  
32 The PV is that obligating events for Social Security, Medicare and RRB occur when  
33 participants substantially meet eligibility conditions and attain fully insured status by  
34 completing sufficient work in covered employment. Obligating events also occur when  
35 subsequent work increases their future benefit (PV pars. A16, A39). The Government  
36 and the participant have an agreement or understanding concerning settlement at that  
37 point (PV par. A39). Thus, the definition is satisfied. At this point economic cost is  
38 incurred the omission of which results in incomplete reporting (PV par. A17).

39  
40 Distinction between “exchange” and “nonexchange” transactions is not determinative.  
41 Expenses may be incurred and liabilities arise equally for exchange, nonexchange, and  
42 quasi-exchange transactions (PV par. A18).

43  
44 Work in covered employment before “fully insured” status is not an obligating event  
45 because participants are not eligible for benefits at that point (PV par. A40).

46  
47 Uncertainty is addressed through measurement (PV par. A39). Measurement uncertainty  
48 can be tolerated if clearly explained (PV par. A67).

49  
50 The PV rationale concludes by noting that the balance sheet and SNC are primary  
51 means of communication (PV par. A100).

1           **Alternative View**  
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3           The AV is that social insurance reporting should be designed to meet its unique nature.  
4           Additional reporting proposed (AV par. 115). Financial reporting should help users  
5           understand and evaluate the:

- 6
- 7           ○ current status and longer-term fiscal sustainability of SI and other programs, as  
8           well as the inter-generational effects and potential effect on individuals' long-term  
9           planning (AV par. A116);
  - 10          ○ impact of the Government's operations on the financial condition of the  
11          Government and the nation, as per SFFAC 1 (AV par. A117);
  - 12          ○ long-term sustainability of federal programs (AV par. A118).
- 13

14          Such reporting should consider indicators of fiscal sustainability, factors affecting federal  
15          costs, sensitivity of the estimates, and many other factors (AV par. A119).

16

17          The AV is that the complex nature of the Government requires an expanded model.  
18          FASAB has provided a model with additional statements that can be articulated, bridged,  
19          or aligned into an integrated framework (AV par. A120).

20

21          SI is a category of program unique to government, usually at the national level, designed  
22          to protect against hazards that might produce large dependency problems (AV par.  
23          A122). SI is compulsory. Participants do not select the kind or amount of protection or  
24          the price (AV par. A123). SI is a pay-as-you-go program (AV par. A125). SI is a  
25          deliberate inter-generational transfer. Little correlation exists between taxes and benefits  
26          (AV par. A126). Nor is SI like private insurance where there is a direct relationship  
27          between risk and premiums paid (AV par. A127); nor like employee benefits that feature  
28          exchange transactions (AV par. A128).

29

30          The AV is that the liability and related expense for SI benefits should continue to be  
31          recognized when benefits become "due and payable" for several reasons, including

- 32
- 33          1. future scheduled benefits are not present obligations,
  - 34          2. recognizing future benefits would result in a mismatch of costs and transfers or  
35          services, and
  - 36          3. amounts are not reasonably estimable given the government's ability to change  
37          the SI laws and the unsustainability of current benefits (AV pars. A133-A137).
- 38

39          SFFAS 5 notes that the distinction between exchange and nonexchange transactions is  
40          important in determining the point of liability recognition (AV par. A135-A136). The  
41          Supreme Court has affirmed the right of Congress to modify law. The Government is not  
42          bound in its policy decision by previous actions (AV par. A137). Nor would it be a liability  
43          under the *Elements* ED because the Government is not committed or bound to make SI  
44          or other benefit payments until all eligibility criteria are met (AV par. A139-A141).  
45          Government costs should be matched year by year with the delivery of services (AV par.  
46          A142).

47

48          SI is like defense and public education: costs that are highly likely to continue but are not  
49          recognized as costs of the current period. They will be financed by future taxes. There is  
50          not present obligation to provide them (AV par. A143).

51

1 In addition, the enormity of the SI “liability” would distort the amounts related to other  
2 activities and render them insignificant (AV par. A144).

3  
4 Given the ability of the government to change the laws and the unsustainability of  
5 current benefits under current financing, amounts are uncertain and not reliably  
6 estimable (AV pars. A133, A145).

7  
8 The Alternative View is that the PV is inconsistent with public sector accounting standard  
9 setters’ opinions (AV par. A110 -A114).

10  
11 IV. IPSASB Update

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13 Staff notes that at its meeting on July 3-6, 2007, the IPSASB decided to issue three  
14 documents following review at the November 2006 meeting. The documents are:

- 15  
16 (1) an exposure draft (“Social Benefits: Disclosure: Cash Transfers”) requiring  
17 disclosure of the present value of cash transfers to those attaining threshold  
18 eligibility,  
19 (2) a consultation paper (“Social Benefits: Issues in Recognition and  
20 Measurement”) seeking input on some key issues in recognition and  
21 measurement of expenses and liabilities related to social benefits,  
22 specifically, when a present obligation arises for cash transfers and the  
23 impact of contributions and earmarked taxes, present obligations for  
24 individual goods and services, and revalidation of eligibility criteria as a  
25 recognition criterion or measurement attribute; and,  
26 (3) a project brief regarding fiscal sustainability.

27  
28 V. Areas Where Board Members’ Views Differ and/or in which Members (or Respondents)  
29 Have Expressed Interest

30  
31 Based on the *Preliminary Views* document and the discussion at the May 23 hearing, the  
32 following are areas where members’ views differ:

- 33  
34 1. The event within social insurance programs that would satisfy the “present  
35 obligation” requirement of the liability definition  
36  
37 2. The effect of current law and Congress’ ability to change current law  
38

39 A key issue regarding “legal enforceability” is the differing views on the effect of  
40 Congress’s ability to change the law. The *Elements* ED, paragraph 44, states  
41 that:

42  
43 To meet the definition of a liability, the federal government’s contract or other  
44 agreement to provide assets or services ... must be based on *existing*  
45 conditions, including current law, because an essential characteristic of a  
46 liability is that the government has a *present* obligation, even if conditions  
47 may change before settlement is due. ... [L]iabilities and all other elements  
48 of accrual-basis financial statements are based on transactions or events  
49 that already have occurred. The government’s power to change existing  
50 conditions does not preclude what otherwise would be a present obligation  
51 and recognized as a liability.

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3. The meaning of “legally enforceable” and/or “legal liability”

Some argue that SI benefits are not “legally enforceable” and/or a “legal liability.” The Board has not defined these terms. Some may view them narrowly to denote a claim enforceable via judicial process immediately or soon. Others may view “legal enforceability” more broadly; for example, a claim eventually enforceable when or if it matures. For example, interest on Treasury debt is payable when it matures. Some claims are contingently enforceable and/or potentially enforceable via judicial process, e.g., insurance claims. SI benefits are payable if the participant lives to be 62 or older, dies with survivors, or is disabled. Other contingent claims include lawsuits and environmental responsibilities.

4. What a “liability” on the balance sheet would or should communicate

5. The appropriate SI cost, e.g., the conceptual difference between (1) the cost of federal employees and other administrative costs and (2) SI costs, if any

6. What other national governments are reporting on accrual financial statements comparable to the FR

7. The effect of reporting a long-term liability on efforts to reform Social Security and Medicare [Note: Members seem to agree that this point is not relevant to the discussion of GAAP.]

8. SOSI format:

- A. PV – SOSI line item links to balance sheet; add section for SOSI changes
- B. AV – retain current SOSI and add a new basic statement analyzing SOSI changes

9. Other:

- A. ?

Staff requests member feedback on the above issues, which it plans to develop along with others to be identified in the future. For example, are these issues of interest to the members? What other issues should the staff develop?

VI. Possible Alternative Approaches

There appears to be a consensus on certain components of a draft social insurance standard. The staff wishes to confirm that there is agreement on these components.

First, the future exposure draft on social insurance accounting should require the current Statement of Social Insurance (SOSI) as well as a statement of changes in SOSI amounts. The exact format for the statement of changes is to be determined.

In addition, sustainability reporting is necessary. There is a separate project on that subject, and the staff assumes that that project will address the subject. However, the

1 members may wish to ensure that the proposal resulting from the separate project  
2 precedes the SI exposure draft.

3  
4 Finally, members agreed that the supplementary information required in SFFAS 17  
5 should be continued.

6  
7 Regarding the basic areas where the members' views differ, the staff suggests the  
8 following alternative approaches for the Board's consideration. They are based on ideas  
9 presented in the *Preliminary Views* document and/or expressed by respondents or  
10 Board members. The staff could develop any of these as the Board wishes:

- 11  
12 1. Primary or Alternative View – One approach, of course, is to adopt either the PV  
13 or AV as presented in the *Preliminary Views* document.
- 14  
15 2. Modify the Primary or Alternative View – Another approach would be to adopt a  
16 modified version of either the PV or the AV. One option associated with the PV is  
17 to conclude that, although the liability definition (in *Elements* concept statement)  
18 is satisfied when participants substantially meet the eligibility requirements for  
19 fully insured status (e.g., 40QC), the second recognition requirement (in the  
20 *Elements* statement) regarding measurability leads to a “threshold liability” for the  
21 balance sheet. The “threshold” obligating event occurs when a participant is  
22 eligible for immediate annuity or survivor or disability benefits, e.g., at 62 or 65  
23 years of age. The *Elements* statement states that measurement may require the  
24 use of estimates or approximations and an assessment of the probability that  
25 future inflows or outflows ... will result from them (*Elements*, par. 7). The  
26 uncertainty and order of magnitude associated with Social Security and Medicare  
27 at 40 QC or equivalent may be considered outside relevant range of the current  
28 balance sheet model. Although the SOSI present values are audited now, they  
29 are presented in financial statement developed for that specific purpose.  
30 Advantages of recognizing the threshold amount include that it is consistent with  
31 the amount that the IPSASB's current exposure draft regarding accounting for  
32 social benefits requires to be disclosed as the liability in the notes. In addition,  
33 this amount ties to current SOSI line items.
- 34  
35 3. Expansion of the Current Reporting Model – The current reporting model can be  
36 expanded, either by adding a new section to the existing balance sheet or  
37 develop a new statement. See Attachment 4 for Table 1 from the executive  
38 summary of the 2006 FR about which respondents have spoken favorably.

39  
40 Reporting different levels of information is similar to the Financial Accounting  
41 Standards Board (FASB) approach regarding “other comprehensive income.”  
42 FASB issued FAS 130, *Reporting Comprehensive Income*, in June 1997. FAS  
43 130 establishes a standard for disaggregated reporting and display of  
44 comprehensive income and its components (revenue, expense, gains, and  
45 losses). In addition, other FASB statements require segregation of  
46 comprehensive income components, for example FAS 158, *Employers'*  
47 *Accounting for Defined Benefit Pension and Other Postretirement Plans—an*  
48 *amendment of FASB Statements No. 87, 88, 106, and 132(R)*.

49  
50 The FASB and International Accounting Standards Board (IASB) are currently  
51 working on a financial statement presentation project the objective of which is to

1 explore ways of presenting information in individual financial statements (and  
2 among the financial statements) that improve the ability of investors, creditors,  
3 and other financial statement users to:

- 4
- 5 ○ Understand an entity's present and past financial position
- 6 ○ Understand the past operating, financing, and other activities that
- 7 caused an entity's financial position to change and the components
- 8 of those changes
- 9 ○ Use that financial statement information (along with information from
- 10 other sources) to assess the amounts, timing, and uncertainty of an
- 11 entity's future cash flows.
- 12

13 Developing additional levels for the federal balance sheet and/of statement of net  
14 cost may be appropriate for the SI project at this time. Additional levels may be  
15 useful in communicating the nature of federal liabilities. For example, liabilities  
16 arising from what have been referred to as "social contracts" by some might be  
17 distinguished from those arising from exchange-related contracts. [Note that this  
18 might be characterized as a "continuum" of liabilities and align with the  
19 "continuum" discussed in item 4 below.]  
20

- 21 4. New Element for the Existing Reporting Model – A new element could be  
22 considered that would be part of net position but not a "liability," e.g.,  
23 "obligations," "commitments," "responsibilities." This approach would develop the  
24 notion of a continuum<sup>3</sup> that some members introduced at the May 23 hearing.  
25 The continuum could be characterized not as a "liability continuum" but as  
26 "responsibility" or other continuum containing all types of federal commitments,  
27 e.g., social welfare, disaster relief, social insurance, other federal insurance,  
28 federal employee benefits, Treasury and other "full faith and credit" federal  
29 securities, and contract obligations.  
30

31  
32 Attachments

- 33  
34 Attachment 1 – Staff Summary of Responses (updated from May 2007 edition)  
35 Attachment 2 – Summary/"minutes" of May 23 hearing  
36 Attachment 3 – Howell Jackson's Proposal  
37 Attachment 4 – Table 1, FR Executive Summary  
38 Attachment 5 – Worksheet re Tabulation of Respondents Comments

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<sup>3</sup> Webster's defines continuum as 1: a coherent whole characterized as a collection, sequence, or progression of values or elements varying by minute degrees ....